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Trading steps

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By Wiley Barbour

A US federal cap-and-trade emissions programme is looking increasingly likely to materialise under the next president. But the country still has a long way to go before it's ready to trade, says Wiley Barbour.

After years of delay, it is finally looking likely that the US government will pass legislation to adopt a cap-and-trade programme to regulate greenhouse gas (GHG) emissions, with both presidential candidates supporting such an approach. Yet, despite progress at state and regional levels, many US companies are still unprepared for mandatory GHG limits and have yet to develop internal strategies for coping with the compliance systems and market forces that accompany cap-and-trade programmes.

For every multinational corporation familiar with the design of the Kyoto Protocol, there are dozens of companies with little or no experience with tradable permits and market mechanisms. Even companies that have participated in voluntary climate initiatives will likely find that a mandatory system requires more rigorous reporting or more accurate and frequent measurement. If things continue on the current path, there is the risk of market failures and a longer period of adjustment within covered sectors following the implementation of the anticipated policy.

But, due to the lack of clear policy signals from Washington, many US-based companies are not ready to make the changes necessary to achieve compliance in an economically efficient manner. Compliance planning begins with an accurate emissions inventory and the development of internal abatement cost curves, but many firms have not yet completed these exercises. Some companies currently purchasing offsets from voluntary markets may find these credits unacceptable under a mandatory system.

Many experts believe that the start of the first compliance period in a US trading programme is at least four years away, allowing for Congress to finalise legislation, the

US Environmental Protection Agency (EPA) to craft regulations, public hearings, legal challenges and a trial reporting period. Delay makes emission limits harder and more expensive when they do come. During the lead-up to the first compliance period, companies need incentives for early action with a degree of confidence that their efforts will be rewarded, or at least not penalised.

There is still time to help these companies prepare for swift implementation of climate legislation – but only if steps are taken immediately to clarify the policy signals from Washington. It is time for new initiatives to prepare US businesses for the direct and indirect impacts of cap and trade. Policy-makers must find ways to move private capital off the sidelines even in advance of the mandatory cap. Project developers and entrepreneurs need some degree of certainty to invest in clean technologies and emission reductions. Actions now to fully address these aforementioned shortcomings will ensure a smoother transition to a cap-and-trade system. The following five steps could ensure efficient and successful implementation of a federal cap-and-trade programme.

- ∞ The current US administration has muddied the waters over the findings of the UN's Intergovernmental Panel on Climate Change, the National Academy of Sciences and its own science agencies, thereby introducing uncertainty and doubt as to the urgency of the problem. As a new administration assumes power next year, it is essential that the findings of leading scientists be heard without interference and censorship by political appointees. A new administration must also ensure that the various federal agencies speak with clarity on the science of global warming and the risks and costs of inaction.
- ∞ The US Congress should immediately pass an early action offsets bill. This should reward investors developing carbon offset projects in advance of the mandatory cap by directing the US EPA to review and validate existing protocols and registries.
- ∞ Under most of the legislative proposals before Congress, the EPA will be the lead agency responsible for administering proposed cap-and-trade programmes. The extent of coverage and the point of regulation varies across bills, with some focusing on upstream sources (eg, petroleum refineries and energy suppliers),

while others seek to regulate downstream emission sources (eg, industrial boilers and cement kilns). In part, the regulatory design is forced by the projected administrative cost and complexity of a downstream cap that regulates tens of thousands of individual emission sources. The EPA should revitalise efforts to provide policy-makers with comprehensive databases of affected facilities while strengthening data sharing and communications between the climate experts in Washington and the agency's air quality regulators in North Carolina and elsewhere.

- ∞ The EPA should launch a follow-up to the successful Climate Leaders programme – perhaps a Climate Leaders pre-compliance programme? This would create a channel of communication between the government and small- to mid-sized companies that are likely to fall under the cap, providing an opportunity for firms to learn how proposed regulations will affect them. The information shared could encourage more businesses to move towards early reductions. This in turn will help the offset market flourish and stimulate the flow of private capital, while further aligning the goals of industry, government and science.
- ∞ The EPA should convene an advisory committee, drawing from NGOs and carbon market experts, to help with the inclusion of offsets in the cap-and-trade programme. This would include registries, which facilitate the review and approval of projects that can immediately deliver emission offsets to the compliance market, avoiding a potential bottleneck and helping to contain costs by ensuring there is an adequate supply of credits available to the market when the programme starts.

The scientists say we can't afford to wait to start reducing GHG emissions, but business leaders argue they can't afford to act without clearer policy signals from Washington. These five steps will help mobilise US companies to reduce their emissions, even in advance of the final promulgation of a cap-and-trade system, and that's something the country really is ready for.